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VIA OVERNIGHT MAIL

June 7, 2005

RECEIVED

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PUBLIC SERVICE
COMMISSION

Ms. Elizabeth O'Donnell
Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
P.O. Box 615
Frankfort, Kentucky 40602-0615

Re: In the Matter of an Assessment of Kentucky's Electric Generation, Transmission and Distribution Needs, Case No. 2005-00042 70

Dear Ms. O'Donnell:

I have enclosed the written comments of Mr. Gregory C. Ficke, President of ULH&P, in response to the Commission's May 11, 2005 Order in this proceeding. Mr. Ficke will appear at the technical conference on June 14, 2005 to summarize these comments and to respond to questions from the Commission and Staff.

Thank you for your consideration. If you have any questions, please do not hesitate to contact me at (513) 287-3601.

Sincerely,

John J. Finnigan, Jr.
Senior Counsel

JJF/sew

cc: Mr. Gregory C. Ficke (with enclosure)
All Parties of Record (with enclosure)

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN ASSESSMENT OF KENTUCKY'S)	
ELECTRIC GENERATION, TRANSMISSION,)	ADMINISTRATIVE
AND DISTRIBUTION NEEDS)	CASE NO. 2005-00090

COMMENTS OF GREGORY C. FICKE

My name is Gregory C. Ficke. I am Vice President of Cinergy Services, Inc., President of The Union Light, Heat and Power Company ("ULH&P") and President of The Cincinnati Gas & Electric Company. I would like to thank the Commission for the opportunity to make these remarks. I also thank Governor Fletcher and the Commission for their work in developing the Strategic Blueprint for Kentucky's electricity generation, transmission and distribution infrastructure, in response to the findings of the Commonwealth Energy Policy Task Force. I am submitting these comments on behalf of ULH&P, and on behalf of Keith Black, who was also invited to submit comments to this panel.

Although the Commission opened the present case in response to Governor Fletcher's executive order to develop the Strategic Blueprint, ULH&P notes that the Commission has been constructively engaged in resource adequacy issues. For example, the Commission proactively addressed transmission resource adequacy in Administrative Case No. 387, where it investigated the adequacy of Kentucky's transmission system following the August 14, 2003 blackout which engulfed the northeast U.S. The Commission has also constructively participated in developing legislation to address merchant generation and transmission siting issues, in the form of KRS 278.700 through

278.716. ULH&P thanks the Commission for its considerable efforts to ensure resource adequacy.

The Commission's May 11, 2005 Order in this case requested commenting parties to address the following questions:

1. What additional information or data, if any, should the Commission consider in developing the Strategic Blueprint?
2. What are the top issues facing the electric power industry in Kentucky over the next 20 years?
3. What barriers exist, if any, to meeting the future investment needs in electric power infrastructure in Kentucky?

I will address each issue in turn. First, ULH&P notes that there is an abundant amount of data available to the Commission regarding future trends in the electric industry, including reports from the U.S. Department of Energy, the Federal Energy Regulatory Commission ("FERC"), regional reliability councils, regional transmission organizations, industry trade associations and media reports. ULH&P knows that the Commission is fully aware of these sources and that the Commission will consult these sources as needed in preparing the Strategic Blueprint.

Second, ULH&P believes that there are several important issues facing the electric power industry in Kentucky over the next 20 years. One important issue is the need for a constructive regulatory climate. During the past several years, the Public Service Commission has used its best efforts to develop a constructive regulatory climate for all participants in the regulatory process. Recently, however, other participants in the regulatory process have advanced arguments which could be viewed as politically

motivated. One example is the allegation of *ex parte* communications following the Commission's order approving new rates in *In the Matter of the Gas and Electric Rates, Terms and Conditions of Louisville Gas & Electric Company and Kentucky Utilities Company*, Case No. 2003-00433 and 2003-00434. ULH&P believes that the regulatory process works best when all participants work together toward constructive solutions which produce a reasonable balancing of all stakeholders' interests, and that the regulatory process suffers when individual participants engage in overly litigious or politically motivated activities.

A second important issue is whether the retail electric market should be deregulated. Retail competition has been adopted by several other states, but the pace of retail competition slowed substantially after a series of well-publicized stumbling blocks including the California energy crisis, the August 14, 2003 blackout and bankruptcy filing by Enron, Mirant and other energy merchant companies. Residential switching has been slow to develop in many states with retail competition. Some states have reversed plans to introduce retail competition. Kentucky customers have enjoyed low retail electric rates, and it is theoretically possible that competition could result in higher rates for Kentucky customers. I therefore suggest that the Legislature and the Commission should continue their present "wait-and-see" approach on how retail competition continues to develop in other states.

Another issue facing the electric power industry involves resource planning. The Commission has demonstrated a willingness to constructively address resource planning issues on a case-by-case basis without imposing rigid and arbitrary one-size-fits-all rules for resource planning, such as requiring that a competitive bidding process precede all

resource planning decisions. An example of the Commission's flexibility is *In the Matter of the Application of The Union Light, Heat and Power Company for a Certificate of Public Convenience to Acquire Certain Generation Resources and Related Property*, Case No. 2003-00252, where the Commission accepted ULH&P's least-cost resource analysis and approved the transfer of three generating plants from CG&E to ULH&P. This enabled ULH&P to obtain low-cost generating facilities which are well-suited to serve ULH&P's customers. ULH&P urges the Commission to continue this constructive approach toward resource planning issues.

In this regard, ULH&P encourages the Commission to actively work with other states, the National Association of Regulatory Utility Commissioners ("NARUC") and the FERC to more clearly define the boundaries of state vs. FERC jurisdiction generation over resource adequacy issues involving transfers of generating plants between affiliates. In a series of recent cases, the FERC has articulated a position where, if states have approved transfers of generating facilities between affiliates, the FERC will not approve the transfer without a hearing, unless a competitive bidding process was used. Some have questioned whether FERC has overstepped its jurisdiction in this area.

On May 16, 2005, NARUC and FERC held a public meeting in Chicago to address resource procurement. The meeting was known as the "Resource Adequacy Forum" and resulted in the formation of a working group that will attempt to develop a set of "best practices" involving resource procurement. ULH&P encourages the Commission to actively participate in this working group, and to help develop practices that will enhance a public utility's ability to obtain generating facilities from an affiliate, where this has been demonstrated to be the least-cost method for procuring power for the

utility's customers. These rules should provide for the FERC to defer to a state commission's approval of a utility's acquisition of a power plant from an affiliate, even if procured without a competitive bidding process, as long as the acquisition is approved by the state regulatory authority and does not result in the utility acquiring market power over generation supply in the region.

Another issue relating to generation supply involves least-cost resource planning, and providing adequate incentives, to allow utilities to use new technology. The electric industry faces uncertainty as to whether carbon dioxide emissions will be regulated; however, it is increasingly apparent that some restrictions will be imposed. As a result, utilities may consider using alternative technologies for new power plants, such as integrated gasification combined cycle ("IGCC"). This would benefit customers by enhancing the diversity of a utility's portfolio of generating assets, and would also reduce carbon dioxide emissions. The Commission should develop reasonable parameters to place appropriate weight on these considerations during the integrated resource planning process. The Legislature should consider laws to fast-track the permitting process and to provide innovative cost recovery mechanisms and financial incentives for such plants, as other states in this region have done.

Generation siting will always be an issue of concern for the electric industry. This will be especially true if alternative technologies such as IGCC or nuclear plants are proposed, because these types of facilities have a greater siting impact than other types of generating plants. As I previously noted, the Legislature addressed the issue of merchant generation siting in 2002 by enacting KRS 278.700 through 278.716. Regardless of whether a utility or a merchant generator is attempting to site a new plant, it is important

that the Public Service Commission and the Kentucky State Board on Electric Generation and Transmission Siting process the applications in a manner that allows the facilities to be constructed promptly, while giving due consideration to the rights of affected stakeholders. Similar issues exist regarding transmission siting.

The electric industry is concerned with how generation and transmission resource planning and siting will be conducted in the future. Before the advent of regional transmission organizations, generation and transmission planning and siting solely involved the utility, the Commission and impacted stakeholders in the utility's service territory. This will change in the future because AEP belongs to PJM, ULH&P belongs to MISO, and there is uncertainty as to the RTO, if any, to which LG&E and KU will ultimately belong. The RTOs' capacity planning rules and pricing plans are still evolving. Additionally, future transmission siting decisions may involve transmission lines that cut across both RTOs. ULH&P encourages the Commission to work constructively with the RTOs to facilitate the prompt resolution of such matters in a reasonable manner.

The electric utility industry also has concerns about its ability to promptly recover its costs for transmission service. Both PJM and MISO have real-time and day-ahead energy markets based on locational marginal pricing ("LMP"). These wholesale transmission markets enhance the reliability of transmission service by using LMP instead of transmission loading relief procedures to mitigate transmission constraints. Unlike past years when transmission investment was relatively steady and periodic general rate cases provided an adequate cost recovery methodology, a utility's costs from an RTO for transmission service could vary substantially from year-to-year, depending

on the extent of transmission constraints. The Commission therefore should approve trackers to allow utilities to recover transmission costs incurred from RTOs. Although ULH&P believes the Commission has the inherent jurisdiction to do so under its general ratemaking authority, the Legislature should also pass legislation to make the Commission's jurisdiction more clear.

Timely cost recovery for distribution system investment is another issue of concern, because some utilities have an aged transmission and distribution infrastructure which will require substantial investment during the next several years. The Commission has constructively addressed a similar issue involving ULH&P's gas operations, by approving a tracker to allow for prompt recovery of the costs of replacing cast iron and bare steel gas mains. The Attorney General has challenged the Commission's jurisdiction to approve such trackers, and the Legislature addressed this matter in 2005 by enacting a new statute which more clearly establishes the Commission's jurisdiction to approve such trackers. ULH&P requests that the Commission and the Legislature give due consideration to approving similar trackers to allow electric utilities to promptly recover the costs of certain distribution system improvements, similar to innovative cost recovery mechanisms approved by other state commissions, because this would allow utilities to invest the necessary sums to upgrade their distribution systems without impairing the utilities' financial condition.

Finally, the Commission's Order requested commentors to address the barriers to future investment needs for Kentucky's electricity infrastructure. I have already addressed this topic in connection with my discussion of future industry issues, so I will

not repeat these points. On behalf of ULH&P, I thank you for the opportunity to address the Commission on these matters.

Respectfully submitted,

THE UNION LIGHT, HEAT AND
POWER COMPANY

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CERTIFICATE OF SERVICE

I hereby give notice that on this 7th day of June, 2005, I have served a copy of the foregoing Comments of Gregory C. Ficke, President of The Union Light, Heat and Power Company, to The Kentucky Public Service Commission and to the following parties of interest, properly addressed as follows:



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